

BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF DELAWARE

IN THE MATTER OF THE	*	PSC Docket No. 07-186
APPLICATION OF CHESAPEAKE	*	
UTILITIES CORPORATION FOR	*	
A GENERAL INCREASE IN ITS	*	
NATURAL GAS RATES AND FOR	*	
APPROVAL OF CERTAIN CHANGES	*	
TO ITS NATURAL GAS TARIFF	*	

**PROPOSED SETTLEMENT**

On this \_\_\_ day of May, 2008, Chesapeake Utilities Corporation, a Delaware corporation (hereinafter "Chesapeake" or the "Company"), and the other undersigned parties (all of whom together are the "Settling Parties") hereby propose a settlement that, in the Settling Parties' view, appropriately resolves all issues raised in this proceeding.

**I. INTRODUCTION**

1. On July 6, 2007, Chesapeake filed with the Delaware Public Service Commission (the "Commission") an application for a general increase in its natural gas rates and for certain miscellaneous changes to its tariff.

2. On the 21st day of August, 2007, the Commission entered Order No. 7255 pursuant to which Chesapeake was authorized to place into effect on September 4, 2007 the entire proposed increase, under bond, and subject to refund as permitted under 26 Del. C. §306(c).

3. On or about December 14, 2007, the Commission Staff (the "Staff") and the Division of the Public Advocate ("DPA"), and certain Intervenors filed their respective testimony.

4. Subsequently, on February 7, 2008, Chesapeake filed its rebuttal testimony.

5. During the course of this docket, the parties have conducted substantial written discovery in the form of both informal and formal data requests. Evidentiary hearings were scheduled to be conducted at the Commission's office in Dover, Delaware, on March 26, 2008 to address the issues in this docket.

6. The Settling Parties have conferred in an effort to resolve all of the issues raised in this Docket. The Settling Parties have agreed to enter into this Proposed Settlement on the terms and conditions contained herein, because they believe that this Proposed Settlement will serve the interest of the public and the Company, while meeting the statutory requirement that rates be both just and reasonable.

## **II. SETTLEMENT PROVISIONS**

### **Rates and Charges**

7. The total base rate revenue increase, including the increase in miscellaneous revenues, should be \$325,000.00. This is an incremental decrease of \$1,570,668.00 below the level of rates that became effective on an interim basis on September 4, 2007.

8. The Settling Parties agree that the rates and rate design set forth in **Exhibit A** attached hereto and incorporated herein by reference are just and reasonable and in the public interest. **Exhibit A** also reflects the Settling Parties agreement on the allocation of non-gas costs and the rate design to collect such costs. Upon approval of this Settlement by the Commission, Chesapeake shall file with the Commission tariff sheets that incorporate the terms and conditions

of this Settlement. As part of this Proposed Settlement, the Company will not implement its revenue normalization proposal at this time. The parties acknowledge that issues relating to revenue decoupling are being addressed in Delaware PSC Regulation Docket 59. The Company reserves the right to submit a revised rate design, on a revenue neutral basis, for Commission approval, to reflect any Commission decisions made in Regulation Docket 59.

9. The Company is authorized to implement the following new Miscellaneous Charges on a prospective basis:

- a. A Connection Charge of \$35.00
- b. A Seasonal Reconnection Charge equal to the applicable monthly customer charge multiplied by the number of months of inactivity.
- c. A Change of Account Charge of \$17.00.
- d. A Failed Trip Charge of \$35.00

10. A cost of equity of 10.25 % for the Company is reasonable and should be adopted for this proceeding. This produces an overall rate of return of 8.91 % with no short-term debt in the capital structure.

### **Depreciation Rates**

11. The Parties agree to the depreciation rates shown on **Exhibit B**. These depreciation rates greatly reduce the accrual for the removal cost component for certain assets, but this Settlement does not prohibit the Parties or the Commission from re-examining this issue in a future base rate case.

### **Margin Sharing**

12. For purposes of establishing the Company's firm revenue requirements in this proceeding, margins from interruptible sales totaling \$574,869 shall be imputed or credited

against the firm customers' base rates. As a result, the firm revenue requirement has been reduced by this amount and the Company shall retain one hundred percent (100%) of all margins from interruptible transportation customers. Existing Interruptible sales customers with a minimum annual usage level of at least 10,000 MCF will be moved to the ITS (Interruptible Transportation Service) tariff and all existing interruptible sales customers with less than the aforesaid minimum usage will be moved to the appropriate firm sales service rate schedule.

13. During the Determination Period, as defined herein, eighty percent (80%) of the margins from upstream capacity release credits and eighty percent (80%) of any off system sales margins shall be credited to the Company's Gas Sales Service Rate Clause, with the Company retaining twenty percent (20%). The capacity release margins associated with the Company's affiliate, Eastern Shore Natural Gas, will continue to be credited 100% to the Company's Gas Sales Service Rate Clause. The parties hereto reserve the right to review these margins, on a prospective basis, after the conclusion of the initial Determination Period (as defined below), subject nevertheless to any lawful adjustments that may be implemented in the context of any future regulatory proceeding, if any.

14. All capacity release credits and off-system revenue margin credits, if any, shall, for purposes of calculating the Company's Gas Sales Service Rate, be allocated among the RS-1, RS-2, GS, MVS, and LVS customers on a volumetric basis and shall not be allocated among the HLFS and Gas Lighting Customers, consistent with the procedures currently followed by the Company.

15. As used herein, "Determination Period" means the twelve-month period November 1 through October 31. This change to the Margin Sharing mechanism shall be effective as of the date of a final Order issued by the Commission.

### **Outside Contractors**

16. The Company agrees to review its Outside Construction Contractor bidding processes and within six (6) months of the final Commission order in this Docket, the Company shall submit a report to the Commission Staff with proposed guidelines.

### **Conservation Programs and Recovery Mechanism**

17. In this docket, the Company sought approval to implement certain conservation and energy efficiency programs and recover the cost of said programs pursuant to an energy conservation cost recovery mechanism. In an effort to minimize duplication of any natural gas programs that may be offered by the Sustainable Energy Utility (“SEU”) and the Delaware Energy Office in the future, the Company will request, in writing, input with respect to any programs each entity proposes to implement, and the associated cost recovery. Chesapeake will provide the parties in this proceeding with written confirmation of the requests and responses within 10 business days of receipt of the response. The Company reserves the right to file with the Commission a new application for approval to implement a recovery mechanism that would allow the Company to recover from ratepayers the costs incurred by the Company relating to conservation and energy efficiency programs offered by the Company.

### **Main Extension Policy and Area Extension Program**

18. The Company’s Main Extension Policy shall be as described in **Exhibit C** attached hereto, and the Company’s Area Extension Program shall be as described in **Exhibit D**. When and if the Company seeks to make any changes to either the Main Extension Policy or Area Extension Program, the Company shall make application to the Commission and provide Staff, the DPA, and DAAEP with notice of said application.

19. With respect to capital projects undertaken by the Company in accordance with the terms and conditions of the Company's Commission approved main extension policies, the Parties hereto acknowledge that the actual economic results of each particular project will differ from the projections relied upon by the Company in making its determination that each project will provide the Company with a return equal to or greater than the Company's authorized rate of return over the life of the project. The Parties agree that in the Company's next base rate proceeding all such incremental capital projects for main extensions in excess of 500 feet proposed for rate base treatment and initiated subsequent to March 31, 2007 (the "Aggregated Projects") will be evaluated in the aggregate to determine if said capital projects earned (in the aggregate) the Company's authorized rate of return over the life of the project. If, in the evaluation of the Aggregated Projects the Commission determines that the Company did not earn a return equal to or greater than the Company's authorized rate of return on the aggregate amount of investment associated with the Aggregated Projects over the life of the project, then fifty percent (50%) of the shortfall (as determined in accordance with Paragraph 21 below) shall be excluded from rate base until such time that the Aggregated Projects meet or exceed the authorized rate of return over the life of the project. If in the evaluation of the Aggregated Projects the Commission concludes that the Company has earned a return equal to or greater than the Company's authorized rate of return over the life of the project, then all of the capital investment associated with the Aggregated Projects shall be included in rate base.

20. The evaluation of the Aggregated Projects shall be based on an internal rate of return model summarizing all incremental main extension capital projects initiated by the Company subsequent to March 31, 2007. Actual information, to the extent available (such as customer build-out and capital costs) shall be substituted for the original estimates. For example,

if the Company files its next base rate proceeding in 2010, a capital project started in 2008 would have two years of actual data substituted for the original estimates. For the remaining years, the original estimates would be included. If the results of this aggregated internal rate of return model demonstrate that the Company earned a rate of return on the Aggregated Projects equal to or greater than the Company's authorized rate of return over the life of the project, there is no shortfall. If the results of this internal rate of return model indicate that the Company did not earn a return equal to or greater than the Company's authorized rate of return over the life of the project, a shortfall will be deemed to exist. The amount of the shortfall, under such circumstances, shall be equal to the amount of the contribution in aid of construction that would otherwise be necessary in order for the Company to have earned its authorized rate of return on the Aggregated Projects. Under such circumstances, fifty percent (50%) of the shortfall would be deducted from rate base.

21. If, with respect to any initial evaluation of any main extension project, the Company departs from the parameters contained in Exhibit C, before proceeding with the project the Company shall file with the Commission Staff (for informational purposes only) a copy of the economic analysis prepared by the Company showing the conditions and assumptions relied upon by the Company. With respect to each such project, at the time of the Company's next base rate case, such projects shall be evaluated in accordance with Paragraph 20 above. However, for these projects, 100% of any such shortfall shall be excluded from rate base until such time as the project shall have earned a return equal to or greater than the Company's authorized rate of return over the life of the project.

22. For purposes of calculating the amount of revenues received by the Company from residential heating customers located in eastern Sussex County, Delaware, as defined in the

Company's natural gas tariff, in any rate of return analysis performed pursuant to the Company's approved internal rate of return model or pursuant to Paragraphs 19 through 21 hereof, the average annual non-fuel revenue per residential heating customer deemed received by the Company shall be equal to \$375 until changed by further order of the Commission.

23. Except as otherwise provided under the Company's tariff, with respect to any future customers who elect to convert from propane to natural gas, the Company agrees that the customer shall be responsible for paying the cost of converting any of the customer's appliances or HVAC equipment from propane to natural gas (including costs related to the internal piping located with the customer's residence or building or costs associated with the replacement of appliances), and any costs paid by the customer shall not be included in the Company's rate base.

### **Transportation Proposal**

24. In this Docket, the Company submitted a proposal to make transportation service available to all commercial and industrial customers (the "Transportation Proposal"). The Company also signaled its intent to pursue, through a multiple phase-in process in subsequent filings, the transition of all residential consumers to transportation service and the exit of the merchant function. The Company's current Transportation Proposal included only Phase One of its unbundling program (the elimination of the current 3,000 annual MCF eligibility threshold for non-residential consumers). The Company presented a general transition outline but did not attempt to design or propose in any detail the subsequent phases of its intended unbundling process. One retail supplier, Washington Gas Energy Services, submitted testimony in support of the Company's Transportation Proposal but suggested certain operational modifications which it believed would improve the Proposal. Commission Staff and the DPA indicated concerns over the Company's full unbundling objective. Given that the Company's rate filing only addressed



Phase One, Commission Staff's principal concern was the inability to review Phase One in the context of a full unbundling program. Of particular concern was the release of Company pipeline capacity entitlements, the utilization of storage assets and the ability of consumers to select a regulated gas supply option. As part of the overall settlement agreement, the Company has agreed to limit expansion of its current transportation service program to certain interruptible and non-residential consumers within the existing eligibility threshold. While the Company remains committed to expanding its transportation service program with a more comprehensive proposal in the future, the Parties agree that for now, except as provided for below, the current usage thresh-holds for transportation service by commercial and industrial customers shall remain at 3,000 MCF per year. The Parties do agree that for purposes of determining whether or not a customer satisfies the aforesaid 3,000 MCF thresh-hold, firm customers with multiple contiguous meters in a specific geographic location with a common owner shall have the right to aggregate the usage for each meter serving the customer. By way of example, an apartment complex (owned by a single owner) with separate buildings or a college campus with separate buildings, with multiple meters connected throughout the apartment complex or college campus in an unbroken sequence, would be eligible to aggregate the usage for each meter serving separate buildings located within the apartment complex or college campus.

#### **Tariff Modifications**

25. In its Application, the Company sought approval for various modifications to its existing Tariff. The Parties agree that the Company shall be permitted to amend its existing Tariff in the manner set forth in **Exhibit E**.

### **Interruptible Balancing Service Rate**

26. The calculation of the Interruptible Balancing Service Rate will be updated and addressed prospectively as part of the Company's upcoming Gas Sales Service Rate application to be filed on September 1, 2008.

## **II. STANDARD PROVISIONS AND RESERVATIONS**

27. The provisions of this Proposed Settlement are not severable.

28. This Proposed Settlement recommends a compromise for the purposes of settlement and shall not be regarded as a precedent with respect to any rate making or any other principle in any future case or in any existing proceeding, except that, consistent with and subject to the provisos expressly set forth below, this Proposed Settlement shall preclude any Settling Party from taking a contrary position with respect to issues specifically addressed and resolved herein in proceedings involving the review of this Proposed Settlement and any appeals related to this Proposed Settlement. No party to this Proposed Settlement necessarily agrees or disagrees with the treatment of any particular item, any procedure followed, or the resolution of any particular issue addressed in this Proposed Settlement other than as specified herein, except that each Settling Party agrees that the Proposed Settlement may be submitted to the Commission for a determination that it is in the public interest and that no Settling Party will oppose such a determination. Except as expressly set forth below, none of the Settling Parties waives any rights it may have to take any position in future proceedings regarding the issues in this proceeding, including positions contrary to positions taken herein or previously taken.

29. In the event that this Proposed Settlement does not become final, either because it is not approved by the Commission or because it is the subject of a successful appeal and remand, each of the Settling Parties reserves its respective rights to submit additional testimony,

file briefs, or otherwise take positions as it deems appropriate in its sole discretion to litigate the issues in this proceeding.

30. The Proposed Settlement will become effective upon the Commission's issuance of a final order approving this Proposed Settlement and all the settlement terms and conditions without modification. After the issuance of such final order, the terms of this Proposed Settlement shall be implemented and enforceable notwithstanding the pendency of a legal challenge to the Commission's approval of this Proposed Settlement or to actions taken by another regulatory agency or Court, unless such implementation and enforcement is stayed or enjoined by the Commission, another regulatory agency, or a Court having jurisdiction over the matter.

31. The obligations under this Proposed Settlement, if any, that apply for a specific term set forth herein shall expire automatically in accordance with the term specified, and shall require no further action for their expiration.

32. The Settling Parties may enforce this Proposed Settlement through any appropriate action before the Commission or through any other available remedy. The Settling Parties shall consider any final Commission order related to the enforcement or interpretation of this Proposed Settlement as an appealable order to the Superior Court of the State of Delaware. This shall be in addition to any other available remedy at law or in equity.

33. If a Court grants a legal challenge to the Commission's approval of this Proposed Settlement and issues a final non-appealable order which prevents or precludes implementation of any material term of this Proposed Settlement, or if some other legal bar has the same effect, then this Proposed Settlement is voidable upon written notice by any of the Settling Parties.

34. This Proposed Settlement resolves all of the issues specifically addressed herein and precludes the Settling Parties from asserting contrary positions during subsequent litigation in this proceeding or related appeals; provided, however, that this Proposed Settlement is made without admission against or prejudice to any factual or legal positions which any of the Settling Parties may assert (a) in the event that the Commission does not issue a final, non-appealable order approving this Proposed Settlement without modifications; or (b) in other proceedings before the Commission or other governmental body so long as such positions do not attempt to abrogate this Proposed Settlement. This Proposed Settlement is determinative and conclusive of all of the issues addressed herein and, upon approval by the Commission, shall constitute a final adjudication as to the Settling Parties of all of the issues in this proceeding.

35. This Proposed Settlement is expressly conditioned upon the Commission's approval of all of the specific terms and conditions contained herein without modification. If the Commission should fail to grant such approval, or should modify any of the terms and conditions herein, this Proposed Settlement will terminate and be of no force and effect, unless the Settling Parties agree to waive the application of this provision. The Settling Parties will make their best efforts to support this Proposed Settlement and to secure its approval by the Commission.

36. It is expressly understood and agreed that this Proposed Settlement constitutes a negotiated resolution of the issues in this proceeding and any related court appeals.

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### **III. CONCLUSION**

IN WITNESS WHEREOF, intending to legally bind themselves and their successors and assigns, the undersigned parties have caused this Proposed Settlement to be signed by their duly authorized representatives.

Chesapeake Utilities Corporation

Dated: \_\_\_\_\_

By: \_\_\_\_\_

Delaware Public Service Commission Staff

Dated: \_\_\_\_\_

By: \_\_\_\_\_

Division of the Public Advocate

Dated: \_\_\_\_\_

By: \_\_\_\_\_

Delaware Association of Alternative Energy  
Providers

Dated: \_\_\_\_\_

By: \_\_\_\_\_

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